BUSINESS CONDITIONS

A REVIEW BY THE FEDERAL RESERVE BANK OF CHICAGO

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Farm Leases—I

Important Improvements Needed

Farm leases are important in Seventh District agriculture. Forty-four per cent of all land farms in the five states of the Seventh Federal Reserve District was operated under lease in 1945, involving nearly 400 thousand separate farm rental agreements and 42 per cent of all farm operators.[1] Although only 28 per cent of the farm operators rented all their land, an additional 14 per cent rented part of the land they farmed.

Many farm leases are written with the assistance and advice of country bankers. Some rented farms are supervised by them. This places country bankers in a strategic position to aid farm owners and tenant operators in the development of more effective farm leasing arrangements.

The ownership of farm land by nonfarmers and the operation of such land by tenants has, at times, attracted much criticism, some justified and some not. Most of the criticism has sprung from the apparent instability in the relationships of many landowners and tenants to the land and to each other. Tenancy has often been associated with the frequent moving of operators from farm to farm, unprofitable farming due to failure to maintain soil productivity or to inadequate farm units, poor living conditions for tenants, and progressive deterioration of the land and its improvements.

Some of the criticism of tenant operation of farms, no doubt, has reflected the general acceptance in the United States of the owner-operated family-size farm as the ideal in farm land tenure. This goal is consistent with our general economic and political institutions. There is general agreement that the way should be kept open for the majority of farm tenants to become farm owners. It is generally recognized, however, that some percentage of the farms not only *must* be rented but *should* be rented.

Renting permits capable individuals with limited capital, but who desire to operate a farm, to obtain the use of adequate land. It enables them to capture for themselves part of the financial return resulting from any exceptional managerial skill they may have without assuming the risk of a large long-term debt and is excellent training for the time when they may wish to assume the responsibilities and risks of landownership. Also, it provides a productive use for the funds of individuals and corporations who are not interested in operating farms but are willing to invest in farm real estate. Many well-informed farm owners are rendering a valuable service to society by providing well developed, efficient-sized farm units for competent tenants. More farm owners of this type would be a decided benefit to the agriculture in many communities. A basic problem then, is the development of farm lease arrangements which will foster the type of farming adapted to the best long-run interests of the owner, the operator, and the public generally. Much progress has been made along these lines.

MANY LEASES ARE INADEQUATE

The major shortcomings of farm leases as they are commonly used today have been enumerated by many students of the subject and commonly include the following: (1) many leases are brief oral agreements with no written memorandum, often resulting in misunderstandings and short periods of tenure; (2) the term of many leases is too short, frequently only one year, and without provision for renewal or advance notice of termination, commonly resulting in "short-run" farming which often is exploitive of soil resources; (3) terms of leases frequently are determined almost entirely by custom in the area and may not be appropriate to the particular farm nor equitable to the tenant and the owner; (4) written leases often are drawn in terms involving unnecessarily complex legal language which is not understood by either the landlord or the tenant; (5) provisions for settlement of disputes which may arise are often lacking; and (6) provision is seldom made for reimbursement of the tenant for unused improvements made by him or of the landlord for the misuse of land or improvements by the tenant.

These shortcomings, as well as others which could be listed, indicate three general requirements for a satisfactory lease. A lease should provide: (1) assurance to a competent tenant that he may continue on the farm for a period of years; (2) for a system of farming adapted to the area and the farm; and (3) an equitable division of the farm income between tenant and owner.[2] The first two of these are discussed below, the third will be discussed in a succeeding issue of *Business Conditions.*

SECURITY OF TENURE IS ESSENTIAL

Each year a limited number of farm operators will find it possible to improve their status by changing to a different farm. It is doubtful, however, if all the moving which takes place is desirable either from the viewpoint of tenant operators, owners, or society generally. In the states of the Seventh Federal Reserve District in 1945, one-fifth of the farm families had been on the farm they then operated for only one year or less; one-third had been on the same farm for four years or less. The average period of tenure of all farm operators was 14 years. However, these data do not tell the complete story. Many tenant operators continue to operate the same farm for a long period of years but at no time during their tenure do they have assurance either that they will continue to operate the farm for the next several years or that

[1]Census of Agriculture, 1945, U. S. Department of Commerce.

[2]The state agricultural colleges in Seventh District states have developed suggested lease agreements which are available to those concerned with this problem.

(*Continued on Inside Back Cover*)

New Farm Program Proposed

Administration Would Raise Farm Benefits

A radically different, if not revolutionary, new farm program has been proposed to Congress on behalf of the Administration by Secretary of Agriculture Brannan. If unexpected and unusual proposals are a fulfillment of implied or explicit campaign promises to farmers, the new program is generally conceded to constitute such a fulfillment.

Into an atmosphere already supercharged by the heat of controversy between the extremes of high level mandatory farm price supports on the one hand and advocacy of lower flexible support levels on the other, the new plan, a closely guarded secret until it was sprung on the House and Senate Agricultural Committees, has dropped like a bombshell. It has provoked a wide range of reaction, running from characterization as "rampant socialism" to "sound and constructive economics." Some aspects of the proposal are so far reaching as to have aroused fears in the minds of able farm leadership alarmed by the great degree of regimentation of farmers which they see implied in the powers requested by and for the Secretary of Agriculture.

Before turning to the specific proposals it may be well to sketch the six point platform or philosophy which the Secretary sets up as a basis for his proposals:

(1) He says that an effective farm program can help prevent depressions by slowing down or checking the declining farm prices, arguing that most depressions have been farm-led and farm-fed.

(2) He would require such a farm program on the grounds that it would help maintain and build markets among farmers for industrial goods and bolster high employment. Under this head he emphasizes that industry today is increasingly dependent on the farm market as an outlet for its products.

(3) He contends that stable farm prices and incomes encourage a high level of farm output with a maximum of assurance of reasonable prices to consumers. This point appears to be based upon the trend of increased production in part stimulated by the exaggerated demands of the war period. On the negative side it can also be argued that unstable farm prices and incomes have not been in our history a deterrent to all-out production on the part of farmers.

(4) The Secretary expresses the belief that maintaining farm income is of vital importance to the conservation of agricultural resources, arguing that low prices and unsatisfactory incomes induce mining the soil, and that price supports can promote conservation by giving farmers a standard of living high enough that they will not need to exhaust their resources, and particularly if properly managed by encouraging types of farming, specifically livestock and livestock products which tend to conserve agricultural resources.

(5) The Secretary holds that an effective farm program is necessary to national security, that it would give a reserve stock of products which would protect the country against crop failure and other sudden emergencies.

(6) He argues that a high level of farm income would safeguard the economic strength of rural people and provide greater individual opportunity for them. For the above reasons the program which he recommends is designed to produce a maximum volume of farm income and purchasing power.

WHAT IS PROPOSED

The new proposal would begin by junking the 1909-14 basis for computation of parity for agriculture. It would also in part dispose of price parity for individual commodities. The new criteria would be on the basis of *income* parity using the average purchasing power of American agriculture for the 10 years *1939 through 1948* as a basis for parity. The gross cash receipts of American farmers during this 10-year period ranged from just under eight billion dollars in 1939 to 31 billion dollars in 1948. In arriving at the new basis these total figures for each year would be adjusted by the index of prices paid by farmers for goods and services used in living and production, including an allowance for interest and taxes, this index to be on a base of 1939-48 equal to 100. After adjusting each year's figures and averaging them there is then obtained an average annual purchasing power of roughly 18 billion dollars for the 10-year period. To get the parity factor for the current year this base of 18 billion dollars is adjusted upward or downward depending upon whether the prices paid by farmers are currently higher or lower than they were on the average in the 1939-48 period. This gives the income support level for the current year. The calculation may be illustrated for figures as of March 15 of this year. Since prices paid by farmers on that date were 44 per cent above the base period, the 18 billion dollar base purchasing power would be increased by 44 per cent giving in the example an income support level for this year of roughly 26 billion dollars. The Secretary suggests that this base period would be shifted along as time passes with about a two-year lag in order to gather, compute, and verify data. Thus the 1939-48 basis would be used for 1950 programs, while for 1951 the base would be 1940-49.

But in order to translate all of this into a manageable form and to get standards for supporting prices, the average of cash receipts for the most recent 10 years would be used in order to get a price factor. Again to illustrate, the average cash receipts for 1940-49 were roughly 21 billion dollars. Since the adjusted income

support level for the current year as indicated above was 26 billion dollars, and since this is 25 per cent above the 21 billion dollar cash receipts averaged for 1940-49, the ratio of income support level to this average of cash receipts would be 1.25. Therefore, to get the current price support standard for a commodity its average price during the 1940-49 period will be multiplied by 1.25.

The Secretary suggests classifying farm products into two groups for purposes of price supports. In the first group would be the storable commodities which account for about 25 per cent of the total of cash receipts and would include cotton, corn, wheat, other grains, tobacco, the oil seed crops, dry beans and peas, wool, and peanuts. The prices of these commodities would be supported as in the past by commodity loans and purchase agreements, or Government purchases. The perishable commodities those which are difficult or impossible to store, including fruits, vegetables, meat animals, milk, butterfat, and poultry and eggs, would be supported in an entirely different manner. These the Secretary would permit to move through regular markets at whatever prices the market would bring. The price supports would take the form of direct payments to the farmer for the amount of difference between the market price and the price support standard.

Using the above methods of calculation the difference between the current levels of support at generally 90 per cent of parity and the supports which would prevail if the proposals were currently in operation can be seen from the accompanying table.

It is to be noted from these figures that aside from modest downward revisions in the support levels of wheat, oats, barley, eggs, peanuts, and oranges the suggested revisions give a generally higher level of support prices than would prevail under the continuation of 90 per cent supports based on current definitions of parity.

Lest it be mistaken from all of the above details that such changes would be an unlimited blessing for farmers, it should be pointed out that there is another side of the coin which was hinted at in the testimony of the Secretary before the House and Senate Agricultural Committees. He said that he did not "believe that full benefits, if any, should be extended to producers who operate without regard to the welfare of the general public or of their fellow farmers." He then went on to mention the increasing yields and production and indicated his belief that high level production would continue and that yields might increase and that, therefore, farmers have to prepare to restrict production of some items to less than maximum capacity. He requested that marketing quotas and acreage allotments continue to be provided as a means of controlling the output of the basic commodities and that they also be made applicable for other commodities such as soybeans, flaxseed, and dry edible beans and for feed grains and rye when in effect on corn. Similar requirements with the addition of marketing agreements and orders were requested for fruits, vegetables, and nuts. He also implied that such devices as marketing quotas might be required for meat animals, dairy products, and poultry and eggs. He suggested that "eligibility of a producer for participation in the benefits of any price support program should be conditioned upon compliance with or adoption of applicable programs of production adjustment, marketing quotas or agreements, and the carrying out of reasonable conservation practice requirements."

PROPOSALS RAISE PROBLEMS

The ramifications and implications of all the aspects of the proposed program cannot be covered within these space limitations. Some of the more obvious aspects can be briefly touched upon.

In view of the changing costs, technology, and shifting demands the 1909-14 parity base, a 35 to 40 year old criterion with all of the fact and fiction, fable and fancy, and stagnant statistics associated with it as a base period is quite obviously out of date and ignores a changing world. Probably only a few producer groups, such as possibly wheat and peanuts, would mourn its passing. A more modern base for parity formulation has long been in order. Unreal results come from the calculation of parity bases for individual commodities no matter what the base period. They have always tended in the direction of divorcing price supports from the operations of the forces of supply and demand.

ESTIMATED ALTERNATIVE SUPPORT STANDARDS FOR 1950 BASED ON PARITY INDEX FOR MARCH 15, 1949

(Amounts in dollars)

Commodity (Grouped according to present legislation)	Unit	Income Support Standard[1]	90 Per Cent Current Parity
Basic commodities:			
Wheat	bu.	1.88	1.95
Corn	bu.	1.46	1.42
Cotton	lb.	.2799	.2745
Rice	bu.	2.26	1.80
Peanuts	lb.	.0945	.106
Tobacco:			
Flue-cured	lb.	.492	.406
Burley	lb.	.496	.393
Specified Steagall commodities:[2]			
Butterfat	lb.	.669	.582
Milk, whole	cwt.	4.22	3.55
Hogs	cwt.	19.00	16.10
Eggs	doz.	.458	.476
Chickens	lb.	.290	.252
Flaxseed	bu.	4.30	3.74
Soybeans	bu.	2.54	2.12
Beans, dry edible	cwt.	8.45	7.46
Potatoes	bu.	1.59	1.62
Other commodities:			
Beef cattle	cwt.	16.90	12.00
Lambs	cwt.	18.40	13.00
Oats	bu.	.825	.884
Barley	bu.	1.22	1.37
Apples	bu.	2.61	2.12
Wool	lb.	.498	.405
Oranges	box	1.96	3.32

[1]1940-49 average prices times 1.25. Prices for 1949 estimated basis current prices and announced or mandatory support levels for 1949.
[2]Sweet potatoes, dry field peas, American-Egyptian cotton, and turkeys are also Steagall commodities.
SOURCE: Statement by Secretary of Agriculture Charles F. Brannan, Exhibit C.

The radical shift to a purchasing power parity appears to come near to the objectives of farm support policy and legislation. If there is to be "a farm program" it should be more effectively implemented so as to achieve its objectives. But in spite of Secretary Brannan's rationalized philosophic basis as discussed in the six points above there is grave question as to whether the citizenry of this country want or can afford to guarantee farmers purchasing power equivalent to the wartime and postwar prosperity of the 1939-48 period. (Secretary Brannan would probably contend that we cannot afford not to guarantee it.) This decade was characterized largely by distorted and exaggerated demands for farm products as a whole and especially for particular farm commodities, giving farm products values materially out of line with normal domestic and world economic conditions. This decade was by all odds the best 10 years of purchasing power ever enjoyed by farmers.

One of the most frequently overlooked and at the same time tragically distinctive aspects of farm support programs is that the more certain, assured, and foreseeable they become the more are they a subsidy to landowners as of the time they are established and the less of benefit are they for the farm family as the years pass. Calculable benefits tend more strongly to be bid into the price of land because of the competition for good farm land. To this extent they become a windfall to landowners and are greatly diluted as a continuing benefit to farm operation.

Much good can be said for the proposed methods of calculating price support standards for individual commodities. They would represent a marked improvement over present methods. Even though a 10-year average is slow to reflect changing conditions they do, nevertheless, permit to some extent the forces of supply and demand to express themselves in the price bases. But if the production payments and other benefits of the proposed program are to be included in the averages for adjusting the support standards they can only make subsidies and the resulting price distortions self-perpetuating by giving statistical sanctification to prices that will have been politically determined rather than reflecting economic factors. This can best be brought out by an illustration that puts the principles to ridiculous extreme. For example, let us suppose that butterfat became so useless in our economy that its market price fell to say five cents per pound for a 10-year average. If the difference between the income support standard of 67 cents per pound and the five cents market price were made up by direct production payments of 62 cents per pound and if in calculating the 10-year average price before adjustment the 67 cents realized by farmers is treated as the price to be averaged, the effect can only be to perpetuate an artifically high price for butter and to continue subsidizing its production at great public expense. If on the other hand the market price of five cents is used in the calculation, the income support standard would continue to fall and along with it the production payments, thus diverting farm resources to more profitable outlets.

There is much good sound sense in the aspects of his proposal dealing with the encouragement of consumption by permitting many products to move into consumption at whatever price the market will bring. In the face of a truly great productive agricultural capacity it seems almost a crime against nature and humanity to throttle production in the name of "orderly marketing."

From the standpoint of human welfare there is also much to be said for the proposal if it will, as the Secretary believes, encourage a high level production and consumption of livestock and livestock products. A minor dissent can be taken from the Secretary's contention that large stocks of feed grains would stabilize livestock production. They could have this effect only if the administrators had the courage and it were politically possible to draw on stocks of feeds whenever needed. We did this in wartime when an emergency made it mandatory and when a rising price level made it possible to show profits on such stocks, but would we do so in the absence of these conditions?

It would appear from the Secretary's statements that the conditions to be demanded of farmers under this proposal have been quite obviously soft-pedaled. The hints of controls from the Secretary's own words have alarmed many observers, justifiable or no, to a fear of degrees and kinds of regimentation and planned economy far surpassing anything previously experienced in this country, probably even in wartime. There can be no doubt that an extensive bureaucracy to handle all the details of implementing these proposals would be required. The question of what would be the cost of such a program is almost unanswerable except that it seems obvious that with higher income support standards and the inclusion of more commodities the program can hardly be expected to cost less than the price supports committed under existing legislation.

The Secretary can hardly be blamed for being vague about estimates of total cost. It is probable that it would take two or three years of experience under the program to get even a general idea of the financial burden to the Federal Government. There is one point however that ought not to need clarification for anyone who can add. The Secretary has given the impression that both farmers and consumers would benefit under his proposed program, the farmers by higher prices and consumers by lower food costs. Nothing has been said to indicate that the benefits for these two groups would fall upon either the general taxpayer or those who would be hurt if inflationary devices are used to finance the program. To the extent that farmers and consumers pay taxes to support the program the benefits to them would be diminished. If they are to benefit ultimately from such a program it must be only because a disproportionate share of the burden will fall on others than farmers or consumers as such.

Finally, it should be recognized that while this proposal goes a long way in correcting some of the defects in the present paraphernalia for jacking up farm income it is, nevertheless, still a very slow and cumbersome device for achieving a happy adjustment or liaison between the social and political assistance to farmers and the driving urgencies of a dynamic economy.

Developments in Social Security—II

Major Changes Proposed

The possibility of major revisions in the existing system of social security is indicated by the current widespread discussion of a number of important proposals. These proposals, mainly those of the President and the Advisory Council on Social Security established by the Senate Committee on Finance of the 80th Congress, stem from the fact that many important policy problems remain unsolved after more than 13 years of social security on a national scale.

Among the most pressing of these problems is that of the degree of protection provided by the social insurance programs, in terms of both gaps in coverage and low benefit levels relative to assistance payments in the public assistance programs. The half of the labor force currently not covered by old-age and survivors insurance and unemployment insurance includes agricultural and domestic labor, employees of nonprofit institutions, employees of the Federal, state, and local governments, members of the armed forces, self-employed persons, and in the case of unemployment insurance, workers employed by small firms. In the absence of insurance protection, the burden of relieving distress caused by income-loss is borne by the public assistance programs which are usually financed out of general taxation. Both the reports of the Advisory Council on Social Security and the Administration's social insurance bill (HR 2893) premise the establishment of contributory insurance programs as the mainstays of the social security system, and advocate the extension of retirement and survivors insurance coverage to the bulk of that part of the labor force now excluded. In addition, the Advisory Council recommends extension of unemployment insurance coverage to approximately seven million persons now excluded.

Benefit levels in social insurance generally are lower than the public assistance payments that would be available in the absence of insurance protection. Moreover, benefits are low relative to previous earnings. Both the Advisory Council and the Administration's proposals contemplate a substantial increase in the ratio of old-age and survivors insurance benefits to past earnings and large increases in maximum payments. In addition, they provide for increased family allowances. The Advisory Council further recommends increases in both the amount and duration of unemployment insurance benefits. A minimum payroll tax rate for unemployment insurance approximately equal to the currently low national average of 1.2 per cent would enable most states to pay higher benefits for longer periods even under very severe economic conditions. With our aging population, the proposed higher benefits in old-age and survivors insurance would require increases in the payroll tax rates and eventually would require supplemental contributions by the Federal Government from general taxation. Higher benefits in social insurance would relieve many states of that portion of their assistance case loads consisting of social insurance recipients who require supplementary assistance.

DISABILITY AND HEALTH INSURANCE

Proposals for the extension of social insurance protection to new fields, particularly disability and health insurance, have received more attention than any other social security problems. On an average day the total number of persons kept from work due to illness and other forms of disability is between 4 and 4.5 million. HR 2893 provides for the establishment of a system of disability insurance fully coordinated with the present old-age and survivors insurance system, except that temporary disability benefits would be computed in a manner similar to that prevailing in state unemployment insurance laws. The Advisory Council recommends a system of permanent disability insurance coordinated with old-age insurance, with the proviso that benefits in the former be substantially less than those in retirement and survivors insurance. The four existing laws providing temporary disability insurance—three state laws and the Federal law for railroad workers—are closely allied with unemployment insurance.

The costs of the state temporary disability programs have been below the one per cent payroll tax rates imposed. The Advisory Council estimates the long-range cost of its proposal for permanent disability at one-tenth to one-fourth of one per cent; the expansion envisioned under HR 2893 probably would cost somewhat more than the Advisory Council's program. Since almost one-fifth of the present public assistance case load is composed of persons dependent due to disability, the added cost of disability insurance would be in part offset by the eventual reduction in the assistance rolls.

The issue of Federal insurance for medical services has been pending for several years. The Federal Security Administration (FSA) estimates that one-half of the families in the United States cannot afford comprehensive health insurance on a voluntary basis; the Administration bill (S.5) proposes to assure medical care services to this sector of the population. The main sources of controversy are the questions of professional freedom and of the cost of the proposal. The latter is estimated by the FSA at four per cent of annual earnings up to a ceiling of $4800 per person, with the Government contributing about one-fourth from general revenues. In part the contributions would substitute for present non-insurance expenditures for medical care, and to that extent would impose a smaller added burden on contributors.

The magnitude of the cost problem is clearer when the total cost of the proposals for expanding the existing

social insurance programs and inaugurating new ones is computed. By 1980 the estimated contribution rate necessary to support the retirement, disability, and survivor system proposed in HR 2893, the proposed health insurance plan, and the existing unemployment insurance programs would equal approximately 15 per cent of payrolls. The costs probably would be met through payroll taxes totaling five per cent each on employers and employees and Government contributions from general revenues equal to an additional five per cent of payrolls.

The question of the methods to be used to relieve possible protracted mass unemployment has been somewhat obscured by the boom conditions of the past few years. The unemployment insurance system as originally conceived is ideally suited to providing for frictional, seasonal, and other types of unemployment not likely to affect very large numbers of workers for extended periods. During the depression period of the 1930's, most of the unemployed were aided by general assistance and work relief programs; unemployment insurance played only a small part because benefits were not paid in most states until 1938. The unemployment insurance system automatically will be the major source of support for many persons in the early stages of a period of large-scale unemployment. However, as more persons exhaust their benefit rights by remaining unemployed for long periods and as additional persons enter the labor market, other means of providing for them will become necessary.

A partial solution which has been proposed at times is the extension of unemployment insurance benefits at the same rates to the same persons for an additional 26 or more weeks. Unless such a system is financed by a separate state-Federal system or by the Federal Government alone, this proposal would require considerably higher payroll tax rates. Both the desirability and feasibility of substantial increases in payroll taxes in periods of declining employment are doubtful. It seems most probable that the recurrence of a severe and prolonged depression would bring about the development of new work relief programs by the Federal, as well as state and local governments. The residual burden on general assistance undoubtedly would be great. It might become necessary to institute a Federal emergency relief program similar to that of the 1933-35 period, with the Federal Government bearing the major share of the costs.

PROPOSALS FOR PUBLIC ASSISTANCE

The emergence during the past decade of a relatively large "hard core" of dependency requiring large expenditures for public assistance even in periods of high levels of income and employment has been among the major causes of the current fiscal difficulties of state and local governments. The failure of the Federal Government to keep pace by increasing its fiscal participation to the same extent as public assistance costs have risen aggravates the problem. The lag in Federal aid has been particularly apparent in two of the four programs. In aid to dependent children, the maximum payments which the Federal Government will match are substantially lower on a family basis than those for old-age assistance. There has been no Federal aid for general assistance since the mid-1930's. These lags will become much more of a problem in any possible period of declining income and employment, since the more neglected programs are more responsive to changes in economic conditions than are the other assistance programs.

The Advisory Council's proposals for the improvement of the public assistance programs would entail the expenditure of approximately 300 million dollars annually for additional Federal aid; much of this new money would be spent on aid to dependent children and general assistance. The Council recommends the extension of Federal financial participation in the former program so that the maximums for Federal matching are equal, on a family basis, to those for old-age and blind assistance. Federal grants-in-aid for general assistance are also recommended, although the grants would be a smaller portion of state-local expenditures below lower maximums than in the other programs. In addition, the Council advocates that the Federal Government pay one-half of medical care costs for recipients in excess of the assistance maximums, up to specified limits.

HR 2892, another Administration bill, proposes the consolidation of assistance programs into comprehensive state systems. Federal participation for all types of assistance would be up to maximums somewhat in excess of those now existing in old-age and blind assistance, and would apply to medical care costs within limits which are similar to those recommended by the Advisory Council. In addition, the Federal Government would make grants-in-aid up to a total of 24 million dollars for the first year for welfare services provided under approved state plans.

A major change in financing is proposed; instead of matching state expenditures to the extent of three-fourths of a specified amount of average monthly payments and one-half of any additional individual payments up to a specified maximum per person, as is done today, the Federal Government would pay a computed percentage of total welfare expenditures, the percentage varying from 40 to 75 and computed on the basis of each state's per capita income. The increase in Federal participation is shown by the following comparison of Federal aid percentages of total assistance expenditures:

	Actual Calendar 1947	Under HR 2892
United States	43.9	55
Illinois	41.9	45
Indiana	53.7	56
Iowa	50.0	60
Michigan	41.2	52
Wisconsin	47.0	55

Under the Advisory Council's proposals, the Federal share would be intermediate between these two, except that it might be higher than under HR 2892 for Illinois. The increases in the Federal share under HR 2892 are greatest in moderate-income states with high current expenditures for aid to dependent children or general assistance.

Prices Decline Slowly

Lagging Sales, Lower Raw Material Costs Promote Reductions

Despite widespread reports of important price reductions among individual goods and services, the general price slide-off since last August's record peak has been quite orderly and at a fairly slow rate. Moreover, the months immediately ahead seem likely to be marked by continuation of the same gradual downtrend for prices generally, although with more products being affected and considerable variation, of course, among many individual items.

During the past eight months consumer prices have dropped roughly three per cent or an average of less than .5 per cent per month. The January-February drop was slightly greater than one per cent, but the fractional rise in March reduced the extent of the over-all decline. The reduction in wholesale commodity prices since last August has been larger, about seven per cent, but still averaging less than one per cent per month. Because slightly higher farm product and food prices outweighed minor declines in other product groups, the all commodities index of wholesale prices increased from 158.1 in February to 158.4 in March. Recent price movements of commodites on the organized exchanges, however, give indication that further at least moderate declines may lie ahead.

Although past history and general reasoning long ago led most business executives to expect record inflationary prices to subside after demand backlogs disappeared and productive expansion programs neared completion, falling prices, nevertheless, are being interpreted in some quarters of this District as a sign of major business distress. The underlying fear is that the downward price trend will not be stopped short of a deep readjustment; current and future policies based upon such fears could be important in their realization.

High and relatively inflexible costs pose difficult problems for business managements confronted with shrinking markets at prevailing prices. Declining sales and competitive price cuts, however, promise to force many reductions in costs, often with adverse effects upon sellers but welcomed by buyers. Consumer response to more than token price reductions during recent weeks strongly suggests that the buying public is willing and able to re-enter markets when offered quality goods at prices it can afford to pay. Industries or firms unable to cut costs in coming months may well expect greatly increased sales-price competition from substitute products and other companies.

WHOLESALE PRICE TRENDS

As measured by the U. S. Bureau of Labor Statistics, wholesale prices of all commodities dropped 6.6 per cent from August 1948 to March 1949. Subsequent weekly indexes show a resumption of the declines during April, following the price firming during March.

Continuous wholesale price declines of six or more months duration and 6.6 per cent or more total drop have occurred only four times previously in the present century. Two of these—the precipitous break of 1920-21 in which prices fell 44 per cent in 13 months; and 1929-33, in which the decline was slower but of longer duration and extent—were manifestations of important downturns in all business measures. The third major decline, from August 1937 through May 1938, resulted in a lesser overall dip in prices—11 per cent—but was accompanied by sharply higher unemployment, especially in durable goods industries. The drop in 1910, however, was smaller and of shorter duration, eight per cent in seven months, and was not accompanied by many other indications of a serious business setback.

Preceding the most recent decline begun last year, the average of all wholesale prices had undergone a practically uninterrupted month-by-month rise from March 1941. The war years of 1943-45 represented the period of most effective price controls and a total rise of only five per cent in the official wholesale price index occurred during these years. Between January 1946 and August 1948, however, a virtually continuous rise of 58 per cent in general wholesale prices took place, interrupted only briefly during the early months of 1947 and of 1948.

Farm products and food, the items in which prices rose most during the upswing, likewise have declined most since last August (see accompanying chart). Despite the stabilizing effects of Government price supports, farm product prices, nevertheless, have declined 10 per cent and food products 14 per cent at wholesale during the last seven months.

Building materials, although exhibiting a rise almost as great as farm products and food during the inflation, have not yet shared importantly in the decline, having dropped only two per cent. Hides and leather products reached their peak price level during January 1948 and had already declined about 10 per cent by August. However, wholesale prices of hides and leather products as well as those of textiles and clothing products have receded only slightly—i.e., 4.0 per cent and 3.5 per cent respectively—since the August 1948 peak for "all commodities." Chemicals and allied product prices have been reduced about nine per cent on the average.

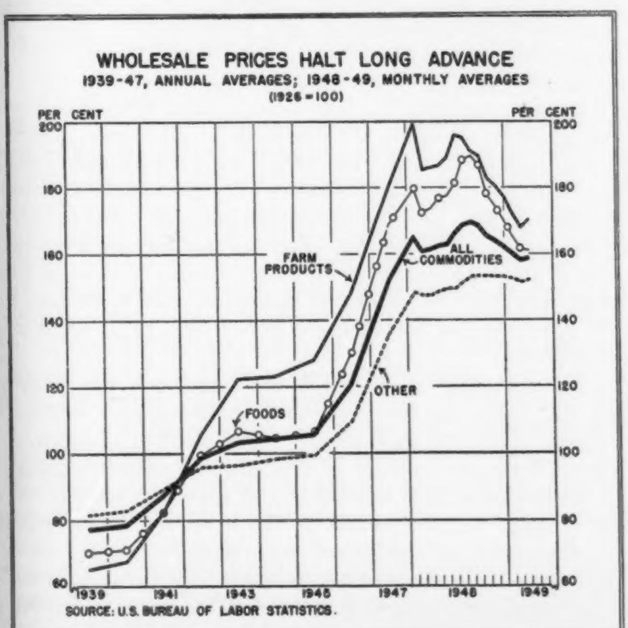
Offsetting these declines in part, price trends in the housefurnishings and metal products lines have continued generally upward but registered small declines during March. Recently announced price reductions for such finished products as floor coverings, furniture, appliances, and automobiles, moreover, probably indicate that trends in these lines now have been reversed.

COST OF LIVING RECEDES

The cost of living as measured by the U. S. Bureau of Labor Statistics Consumer Price Index (CPI), is down about three per cent from the August 1948 peak. The latest official CPI showed cost of living in March to be 169.5 per cent of the 1935-39 average. Judging by the declines already recorded in wholesale prices, the current month's index when published almost certainly will be below the March level, and still further below May a year ago, when the index stood at 170.5.

From the prewar year of 1939 to last year's peak, prices paid by consumers in the Seventh Federal Reserve District's major cities increased somewhat more than the average for all major cities in the nation, but the subsequent price decline has been somewhat greater. Specifically, the average increase for the District's four major cities was 79 per cent from 1939—a period when average District prices were almost identical with the national average—to August 1948. During the same period the increase in the 34 major cities in the nation was 75 per cent. The average decline in the District's major cities since August 1948 has been 3.9 per cent compared with 3.1 per cent for the nation.

The apparent discrepancy between the amount of increase and subsequent drop since the prewar period for wholesale prices (up 110 per cent, then down 6.6 per cent) as compared with consumer prices (up 75 per cent, then back three per cent) is explainable largely in terms of the differences between what the two indexes purport to cover. The CPI, by which changes in cost of living for the typical moderate income family are measured, contains household rents, which have been maintained at low levels through Government controls. Moreover, the CPI also measures personal services such as medical and dental care, barber and beauty service, and street transportation, for which no comparable wholesale concepts exist.



Since the official CPI bases housing cost upon tenancy rather than home ownership—plans for removing this limitation are now being made—it currently fails to reflect the increased shelter cost for families which have purchased homes at inflated postwar prices both in the District and in the nation. Likewise, it cannot reflect the housing cost of individual families which have moved into new uncontrolled apartments because of the very small proportion of such cases. Moreover, since only the major cities are covered for all items of consumer expenditures—indexes of food prices are maintained for some smaller cities—the trends of general consumer prices in the outlying cities of the District are not now measured.

DEFLATION SETS IN

Accompanying the buying resistance already exhibited by consumers in their reactions to prices of finished products is the tendency of industrial buyers to resist high prices of raw materials. With steel and nonferrous scrap leading the field, several primary metal prices have declined in recent weeks largely because of buyer resistance and expanding supply. Lead, zinc, and more recently, copper—all have undergone price reductions in the last two months ranging from more than 35 per cent in the case of lead to about 23 per cent for copper. Similar price weaknesses have developed in fats and oils, industrial chemicals, and textiles, and appear to be in the offing for building materials, and hides and leather products. Overall demand appears to have weakened on a broad front, but supplies of salable goods and services are generally becoming very ample, relative to demand at current prices. Shortages in the sense of wartime and early postwar years are virtually nonexistent, although temporary and localized conditions of short supply for certain items can be found and others might well occur in the months immediately ahead.

In addition to changing supply-demand relationships, income prospects are more limited for the period ahead than a year ago. Declining nonagricultural employment, combined with elimination of overtime and some shortening of basic work week, already have resulted in lowered income paid as wages and salaries, placing many family budgets under even greater pressure. Generally less favorable profit prospects point to smaller incomes for proprietors of business and dividend receivers. Official estimates of farm receipts in 1949 portend a 10 per cent drop in agricultural income as well this year.

Thus, one of the most significant factors affecting current and future trends of prices, both at the wholesale and consumer levels, seems to be the growing reluctance—not to mention inability—of more and more business firms and consumers to spend for other than the basic requirements. As previously pointed out, resistance to high prices initiated by consumers has spread to business managements in making their own purchase commitments. The degree to which this reluctance to spend further develops, and the time period over which it continues, will largely determine how far and how fast the present price slide-off will go.

Declining propensity to spend has extended over a longer period than that of the actual price decline. The U. S. Department of Commerce reports that total private spending declined from 95 per cent of total disposable income in 1947 to less than 91 per cent in the fourth quarter of 1948. Preliminary indications from current income, sales, and savings trends are that the decline has pursued an even greater rate during 1949. Furthermore, downward trends in commercial, industrial, and agricultural loans, accompanied by recent declines in consumer credit reveal an unwillingness of both business and consumers to borrow funds for current spending to the extent which prevailed in the earlier postwar years. Falling prices, moreover, have reduced the financial requirements to handle a given volume of sales or purchases.

As spending declines for any reason, the "next round" of income also tends to shrink either through reduced profits or smaller wage and salary income as a result of the lower sales volume. In addition, when business activity begins to subside, personal savings generally start to rise at least temporarily, a development quite apparent since at least mid-1948. So long as the spending of other consumers, business firms, or Government continues at a high enough level, stepped-up savings of individuals hesitating to buy is offset, and income will continue high. However, whenever increased savings are not fully offset directly or indirectly, smaller incomes, added unemployment, and lower prices almost inevitably follow.

Thus, one immediate problem confronting business is to find means of attracting consumers back into the markets in greater volume. This can only be done by offering and publicizing combinations of price and quality which will stimulate total spending. Reductions which appear to buyers as token cuts will merely cause them to await further declines and not bring about the desired results. But if consumer goods prices are to recede in an orderly manner to a lower but more stable level, business firms which supply raw and semi-finished products to other firms also must adopt comparable price policies which will permit continuing lower costs on finished goods.

Unit labor costs also must come down, preferably by means of increased productivity per man-hour reflected in lower prices for the ultimate consumer. Understandably, no seller rushes to reduce prices, particularly when such action means concomitant inventory losses. If underlying demand-supply conditions, however, will not support prevailing prices, it would seem prudent to make adjustments in a forthright fashion rather than wait until badly weakened markets cause a sharp break in prices.

GENERAL PRICE OUTLOOK

Despite the strong current trend toward lower prices, potentially inflationary influences have not disappeared completely from the scene, and promise to exert a retarding influence upon future price declines. Government spending programs—state and local as well as Federal—now in the planning and/or early development stages, seem likely to have buoying effects similar to those which added to the upward spiral in 1947 and 1948. These programs include not only the well publicized arms to Europe and agricultural support proposals of the Federal Government, but voluminous public works, including resources development projects. Private expenditures, however, are now falling, and new strength from Government spending promises to be an offset to private spending weakness rather than a powerful supplement to private inflationary tendencies as earlier. There is doubt, moreover, that Government planning for the new spending programs has advanced sufficiently for them to exert much appreciable *new* influence on business activity or prices this year.

A very large volume—although below recent record levels—of private expenditures for modernization of plant and equipment seems likely to continue, and indeed may well increase as adjustments in building costs are made and other aspects of the emerging general cost-price structure become clarified. Potential cost reduction in itself is one of the principal stimulants to private capital expenditures. Furthermore, the long-run increase in population, anticipated further rising living standards, and the advent of the new industries—television is but one obvious example—all point to expanded markets helping to maintain higher average levels of employment, income, and prices than existed in the prewar years.

Declining price and employment trends have removed much of the pressure for fourth-round wage demands, but moderate increases, in some industries at least, still seem probable. In any event, wage rates constitute a relatively inflexible item of cost which tend to support rather than reduce prices.

Price declines from the artificially high and distorted levels of record peacetime inflation clearly are under way and seem almost certain to continue throughout the remainder of the year. Never in the past have prices been leveled for any extended period at the peak of inflation; nor is such a development likely now. Nevertheless, a downturn in prices does not necessarily mean an abrupt drop from peak inflation to deep deflation. The slow and extended slide-off to date, in fact, seems to offer some evidence that the domestic and foreign demands on the productive resources of this District and the nation are too great to permit a general price collapse soon. Rapid completion of physical industrial reconversion from war to peace, the continuing threat of war, the relative absence of speculation, and the operation of price support programs—together with the expectation of comparatively heavy and continuing private and public demands for goods and services at proper prices—appear to minimize the possibility of a recurrence of a severe price break as in 1920-21.

Price declines to date for the most part have been gradual, reflecting both the waning influence of inflation and the underlying strength of private and public expenditures. Much can be done to continue the orderly pattern of further price cuts if pricing and spending policies are based upon full recognition of the basic economic forces of adjustment at work, and not merely upon the view that any price movement which is not "up" is tantamount to saying a price collapse is at hand. Consumers are having their first price relief in years and responding well.

FARM LEASES—I

(Continued from Inside Front Cover)

they will be paid for investments in crop and livestock production operations which carry over for several years should they be displaced in the interim. Leases which fail to provide assurance to the tenant that he may continue to operate the farm for a period of years promote exploitive and inefficient farming.

It should not be inferred, however, that this problem is limited to tenant-operated farms alone. Many owner-operators, particularly those laboring under a heavy debt burden or those operating inadequate units, have at times experienced great insecurity of tenure with similar results to farm resources. Also, it should be recognized that providing for security of tenure on farms will not automatically result in adoption of the best livestock, crop, and soil management practices. Ignorance and custom would still continue as major obstacles to the rapid adoption of improved farm practices. However, since most good farm plans in the Seventh District states involve crop and livestock production programs which cannot be brought to maturity for several years, the provision of a relatively high degree of security of tenure is a necessary prerequisite to the adoption of the most appropriate production programs on the farms of the area.

Unfortunately, insecurity of tenure and the many ramifications of this problem would not be solved simply by writing all farm leases for terms of five, ten, or more years instead of for one year as is common now. Many landlords and tenants have only a brief acquaintance with one another at the time they enter into a lease. If the arrangement should prove unsatisfactory to either of them a long-term commitment would be a decided disadvantage in bringing the arrangement to a close. Some owners of farmland are holding the property for sale at the first favorable opportunity and do not wish to handicap the possible sale with a long-term lease. Nor is the inhibition against long-term leases entirely on the side of the landowner. Some tenants do not wish to "tie" themselves to a particular farm for a period of years in case they should have opportunity to rent a better farm or to improve their circumstances in some other manner. Finally, a lease for a specified number of years without provisions for renewal involves the same difficulties as the annual lease but at less frequent intervals.

A workable solution apparently is found in the writing of leases initially for relatively short periods, possibly one, two, or three years, but including provisions: (1) that the lease will be renewed from year to year so long as the tenant operates the farm in a husbandlike manner; (2) that in case the lease is terminated by either party some minimum period of notice must be given and that the tenant will be given full credit for any unused improvements he has made to the farm at his own expense; (3) that the landowner would be compensated for any unusual deterioration of land or improvements resulting from negligence of the tenant.

In addition to providing competent tenant operators with greater permanence of residence in the community, such arrangements permit them to employ their capital and managerial ability to full capacity. They can plan for continuity of operations which is very important if a good program of soil management is to be maintained on the farm. While the provisions do not guarantee the tenant against displacement, they do assure him that he will not be displaced without some minimum period of notice which would permit him to arrange for another farm. Also, he is assured of reimbursement for investments he may have made in the crop and livestock production program on the farm if displaced before full benefit has been received. The types of thing for which the tenant may claim compensation, as well as the rates to be paid, may be listed in the lease. The objective is to provide conditions for tenant operators which will permit and encourage them to organize and operate farms as though they were to spend their lifetimes there. If achieved, the landowner would benefit from the superior farming and the conservation or improvement of his capital investment.

ADAPTED FARMING BENEFITS ALL

Lease provisions should facilitate development of the type of farming adapted to the soil resources of the farm. The soil largely determines an appropriate cropping system. The cropping system, in turn, is an important factor determining an appropriate livestock program. It is important that the operator plan the farm operation from the long-run point of view. This will assure proper attention to such things as the application of lime and phosphate, maintaining good crop rotations including at least minimum acreages of legumes, provision of necessary fences and minor buildings for effective livestock production, and the return of manure and crop residue to the fields.

Improvements such as buildings, fences, drainage, and the like, may be inadequate to permit development of the enterprises which would provide the greatest sustained yield from the farm. The responsibilites of both owner and tenant relative to the provision and maintenance of needed facilities and equipment should be outlined.

Many farms are too small or too "run down" to provide income sufficient for a tenant and to pay rental to the owner, often resulting in overcropping and further deterioration of the soil. The capacity of such farms must be increased either by the addition of land or by stepping up the productivity of the land if good farming and satisfactory owner-tenant relationships are to be obtained.

Not all the essentials for the development and maintenance of good farming can be covered in detail by the provisions of written leases. It is important, therefore, that an understanding of the value of fair and reciprocal arrangements to land operation be built up between owner and tenant. This can be done best where they both have a thorough knowledge of farming and a sincere interest in maintaining the farm unit as an efficient business. Where the owner does not have a good knowledge of farming or is far removed from the farm, employment of competent management to represent his interest is often desirable.

SEVENTH FEDERAL

RESERVE DISTRICT